MULTIMEDIA UNIVERSITY

STUDENT ID NO

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# MULTIMEDIA UNIVERSITY

# FINAL EXAMINATION

**TRIMESTER 1, 2018/2019**

## PPE0054 – BASIC MACROECONOMICS

(Foundation in Business)

13 OCTOBER 2018
2.30 p.m. – 4.30 p.m.
(2 Hours)

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**INSTRUCTIONS TO STUDENT**

1. This question paper consists of **NINE** pages.
2. Answer **ALL** questions in **Section A** and **B**.
3. The answers for **Section A** should be shaded on the OMR sheet. The answers for **Section B** should be written in the Answer Booklet.

## SECTION A: MULTIPLE CHOICE QUESTIONS [30 MARKS]

**Instructions:** Answer **ALL** questions in this section. Shade the answers on the **OMR** sheet.

1. The unit of account is defined as _____.
   A. the medium of exchange
   B. an object that is accepted in return for goods and services
   C. an agreed upon measure for stating prices of goods and services
   D. the exchange of goods and services directly for other goods and services

2. Lucy just sold her economics text books for RM200 cash and deposited the cash that she received in her checking account. This transaction has _____.
   A. increased the quantity of M1
   B. increased the quantity of M2
   C. decreased the quantity of M1
   D. not changed either M1 or M2

3. The central bank influences the interest rate by using which of the following tools?
   i. open market operations
   ii. taxes on bank accounts
   iii. changes in required reserve ratios
   A. i only
   B. iii only
   C. i and iii
   D. i, ii and iii

4. As the central bank, Bank Negara Malaysia (BNM) provides banking services to _____.
   A. the government and the stock market
   B. individuals and controls the quantity of money
   C. banks and regulates financial institutions and markets
   D. banks and determines how much the government will borrow

5. When the central bank purchases government securities, _____.
   A. excess reserves in the banking system increase, leading to more loans being made
   B. required reserves in the banking system increase, leading to more loans being made
   C. excess reserves in the banking system decrease, leading to fewer loans being made
   D. required reserves in the banking system decrease, leading to fewer loans being made

**Continued...**

6. When Ronnie deposits RM20,000 cash in his checkable deposit at the CIMB bank and the CIMB bank's required reserves increase by RM5,000, the required reserve ratio is _____.
   A. 5 percent
   B. 75 percent
   C. 20 percent
   D. 25 percent

7. Suppose that the equilibrium nominal interest rate is 6 percent and the equilibrium quantity of money is $3 million. At any interest rate above 6 percent, _____.
   A. more than $3 million will be supplied and bond prices will fall
   B. less than $3 million will be demanded and bond prices will fall
   C. more than $3 million will be supplied and the interest rate will rise
   D. less than $3 million will be demanded and bond prices will increase

8. The transaction demand for money comes mostly from the fact that _____.
   A. money is a store of value
   B. money is a unit of account
   C. money is a medium of exchange
   D. money has low opportunity cost

9. Suppose that the CPI in Australia was 310 in 2008 and 387.5 in 2009. The inflation rate between those two years was _____.
   A. 6 percent
   B. 12 percent
   C. 25 percent
   D. 35 percent

10. The costs associated with recalculating prices and printing new price lists when there is inflation are known as _____.
   A. menu costs
   B. shoe leather costs
   C. chain-index costs
   D. diminishing costs

11. Under which of the following conditions would you prefer to be the lender?
   A. The nominal rate of interest is 5% and the inflation rate is 1%.
   B. The nominal rate of interest is 12% and the inflation rate is 9%.
   C. The nominal rate of interest is 20% and the inflation rate is 25%.
   D. The nominal rate of interest is 15% and the inflation rate is 14%.

12. The labour force is defined as _____.
   A. all individuals who are currently employed
   B. all individuals who are at least 16 years old and are currently employed
   C. all individuals who are at least 16 years old and are currently employed or unemployed
   D. all individuals who are at least 16 years old and are employed, looking for work or not looking for work

**Continued...**

13. To move to a point on the short run Phillips curve where unemployment is lower, _____.
    A. inflation must fall
    B. the government could increase taxes
    C. the central bank could increase the money supply
    D. none of the above are correct

14. Which of the following describes a situation in which the person is hurt by inflation?
    A. a retiree whose pension is adjusted for inflation
    B. a person who is paid a fixed income during an inflationary period
    C. a person who lends money during a period when inflation is over-predicted
    D. a person who borrows money during a period when inflation is under-predicted

Refer to ***Exhibit 1*** for questions no.15 and no.16. ***Exhibit 1*** shows answers given by people interviewed in the Population Survey.

| | |
|---|---|
| **Person A** | Now that the kids are in school for a full day. This person is looking for work and has been interviewed for three jobs during the past two weeks. |
| **Person B** | This person has been laid off from a job but expects to be called back in two weeks as soon as the economy improves. |
| **Person C** | This person has just graduated from college and will start a new job in three weeks. In the meantime, this person will tour the great Australian beaches. |
| **Person D** | This person was laid off last year when new equipment was installed at the plant reducing the number of workers needed at the plant. |

***Exhibit 1***

15. Refer to ***Exhibit 1***. Which person(s) is (are) frictionally unemployed?
    A. Person A and person C.
    B. Person B.
    C. Person C and person D.
    D. Person B and person C.

16. Refer to ***Exhibit 1***. Which person(s) is (are) structurally unemployed?
    A. Person A and person C.
    B. Person B and person D.
    C. Person C and person D.
    D. Person D.

17. When a country allows trade and becomes an exporter of a good, which of the following would **NOT** be true?
    A. The price paid by domestic consumers of the good increases.
    B. The price received by domestic producers of the good increases.
    C. The losses of domestic consumers exceed the gains of domestic producers.
    D. The gains of domestic producers exceed the losses of domestic consumers.

**Continued...**

18. The combination of goods a nation can consume after trade and specialisation begins is illustrated by the _____ curve.
    A. supply
    B. demand
    C. production possibilities
    D. consumption possibilities

19. When considering the production of two goods, absolute advantage means that one nation _____ produce _____ at lower opportunity cost than its trading partner.
    A. can; both goods
    B. can; only one good
    C. cannot; both goods
    D. none of the above answers is correct

20. If the Malaysian government places a quota on luxury cars, it is to _____.
    A. restrict the quantity of luxury cars that can be imported
    B. increase government revenues from imports of luxury cars to Malaysia
    C. limit the quantity of luxury cars that Malaysia car producers can sell abroad
    D. all of the above

21. The terms of trade are the _____.
    A. exchange rate for two nations
    B. opportunity costs of production
    C. trade negotiations between nations
    D. rate at which two goods will be exchanged

22. If country A has a comparative advantage over country B in the production of a good, this implies _____.
    A. that country A should acquire this good by trading with country B
    B. that country B could not benefit by engaging in trade with country A
    C. it requires fewer resources in country A to produce the good than in country B
    D. the cost of producing the good in terms of some other good's production that must be sacrificed is lower in country A than in country B

23. Major components of the current account are _____.
    A. merchandise exports, merchandise imports, net investment income and net unilateral transfer abroad
    B. outflow of foreign capital, inflow of foreign capital, net investment income and statistical discrepancy
    C. exports of goods and services, imports of goods and services, net investment income and inflow of foreign capital
    D. exports of goods and services, imports of goods and services, net investment income and net unilateral transfer abroad

**Continued...**

24. Which of the following statements is **TRUE**?
    A. A country runs a capital account deficit if it imports more than it exports.
    B. If the current account is in surplus, the capital account must be in deficit.
    C. The overall sum of all the entries in the balance of payments must be positive.
    D. A country runs a current account surplus if it sells more of its assets abroad than it buys abroad.

25. Exports _____.
    A. bring foreign exchange, and thus they are registered as credit in the balance of payments
    B. bring foreign exchange, and thus they are registered as debit in the balance of payments
    C. cause foreign exchange to leave the country, and thus they are registered as debit in the balance of payments
    D. cause foreign exchange to leave the country, and thus they are registered as credit in the balance of payments

26. More Malaysian companies start to invest in Japan. This will lead to a(n) _____.
    A. increase in the supply of yen and a decrease in the demand for ringgit
    B. increase in the demand for yen and a decrease in the supply of ringgit
    C. increase in the demand for yen and an increase in the supply of ringgit
    D. decrease in the demand for yen and an increase in the demand for ringgit

27. The lower the U.S. dollar price per yen, the _____ Japanese goods are for Americans and the _____ Japanese goods Americans will buy; thus _____ yen will be demanded.
    A. less expensive; more; more
    B. less expensive; more; fewer
    C. more expensive; more; fewer
    D. more expensive; fewer; fewer

28. Under a fixed exchange rate system, if ringgit was overvalued, then there would exist _____.
    A. a surplus of ringgit.
    B. a shortage of ringgit.
    C. the equilibrium level of ringgit.
    D. there is not enough information to answer the question.

29. A Malaysian good with a price tag of RM1,000 costs S$525. The exchange rate must be _____.
    A. RM1.50 = S$1
    B. RM1.90 = S$1
    C. RM2.20 = S$1
    D. RM1.25 = S$1

**Continued...**

30. If ringgit appreciates against the Japanese yen, _____.
    A. Malaysia exports to Japan would become less expensive
    B. Malaysia exports to Japan would become more expensive
    C. Japan's imports to Malaysia would become more expensive
    D. all of the above

## SECTION B: STRUCTURED QUESTIONS [70 MARKS]

**Instructions:** Answer **ALL** questions in this section. Write your answers in the Answer Booklet.

*Question 1*

**Part A**

Suppose the central bank purchased RM200,000 of government bonds from you. Assume that you deposited the RM200,000 in Bank of Commerce.

a) Show this transaction on Bank of Commerce's balance sheet.

(1.5 marks)

b) After depositing RM200,000, but before any other actions,
    i. how much is the bank's required reserves and excess reserves if the required reserve ratio is 10 percent.

(4 marks)

    ii. what is the maximum amount of loan that can be given out by Bank of Commerce from this deposit?

(1.5 marks)

    iii. show Bank of Commerce new balance sheet if the bank loan out as much as they can.

(2 marks)

c) What is the value of deposit multiplier?

(1.5 marks)

d) After infinite rounds of depositing and lending, what is the maximum increase in money supply from the central bank's action?

(2 marks)

e) If during the rounds of depositing and lending, some people keep extra currency and fail to deposit all of their receipts, will there be more or less money created from the central bank's action than you found in part (d)? Why?

(1.5 marks)

**Part B**

a) Use the money demand and money supply model to show the money market is in equilibrium with an interest rate of 5 percent and the quantity of money of $800 billion.

(4 marks)

b) Suppose the central bank increases the money supply to $850 billion.
    i. Show the increase in money supply in the diagram drawn in (a)

(1.5 marks)

**Continued...**

ii. If the interest rate remains at 5 percent, will households and firms now be holding more money or less money than they want to hold, and will they be buying or selling short-term financial assets? Explain what will happen to the equilibrium nominal interest rate

(3 marks)

## Part C

***Exhibit 2*** shows data collected in the household survey for November, 2013. The working-age population, employment, unemployment, and labour force are measured in thousands. Calculate the missing values in ***Exhibit 2***. Show your workings.

| | |
|---|---|
| Working-age population | 235,900 |
| Employment | |
| Unemployment | |
| Unemployment rate | 9.4% |
| Labour force | |
| Labour force participation rate | 65.5% |

***Exhibit 2***

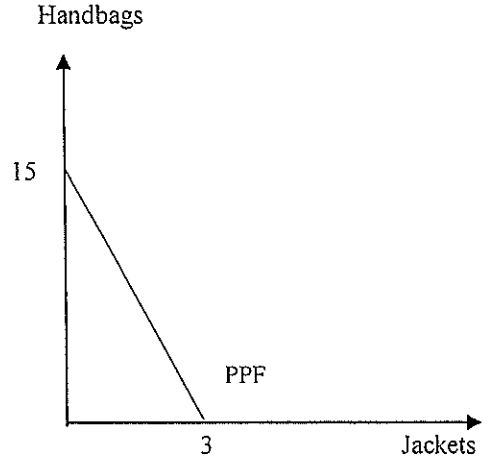
(7.5 marks)

**[TOTAL 30 MARKS]**

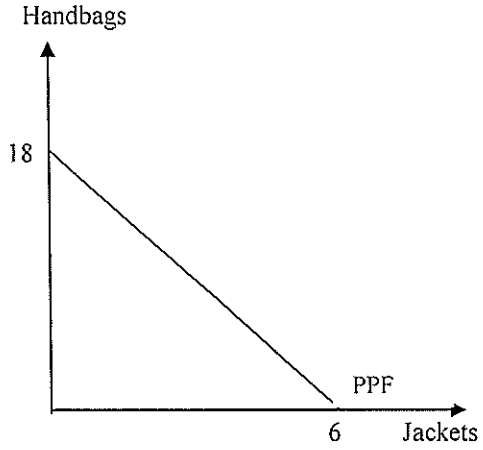
## *Question 2*

## Part A

Consider two countries, Cambodia and Thailand, each capable of producing handbags and jackets. Assume that for each labour employed, the production possibilities frontiers (PPF) for these two countries are as shown in ***Exhibit 3***




***Cambodia***




***Thailand***

***Exhibit 3***

**Continued...**

a) What is the opportunity cost of producing each handbag in each country?
(2 marks)

b) What is the opportunity cost of producing each jacket in each country?
(2 marks)

c) Which country has a comparative advantage in handbag's production? Which country has a comparative advantage in jacket's production? Briefly explain.
(2 marks)

d) Suppose each country has 5,000 workers. Currently, each country devotes 40 percent of its labour force to handbag's production and 60 percent to jacket's production. What is the output of handbags and jackets produced by each country?
(2 marks)

e) Suppose each country specialises in the production of the good in which it has a comparative advantage. What is the number of handbags and jackets produced by the two countries?
(2 marks)

f) Suppose both countries specialise in a good for which they have the comparative advantage and trade 8,000 jackets for 42,000 handbags. What would be the consumption bundles of handbags and jackets after trade for both countries?
(2 marks)

## Part B

*Exhibit 4* shows demand and supply schedules of canned plums in Canada.

| Price ($) | Quantity demanded | Quantity supplied |
|---|---|---|
| 4 | 1200 | 0 |
| 6 | 1000 | 200 |
| 8 | 800 | 400 |
| 10 | 600 | 600 |
| 12 | 400 | 800 |
| 14 | 200 | 1000 |
| 16 | 0 | 1200 |

***Exhibit 4***

a) In the absence of trade, what would be the equilibrium price of canned plums and the level of production in Canada?
(1 mark)

b) If the world price of canned grapes is $8 per can and Canada engages in trade, does Canada import or export canned plums? What is the quantity imported or exported?
(2 marks)

c) Calculate the value of consumer surplus before and after trade.
(2 marks)

d) Calculate the value of producer surplus received by the producers before and after trade.
(2 marks)

e) If trade is allowed, who gains and who losses, the consumers or the producers?
(1 mark)

**[TOTAL 20 MARKS]**

**Continued...**

*Question 3*

**Part A**

***Exhibit 5*** describes the economy of Country X in year 2010.

| Item | $ (million) |
|---|---|
| Merchandise exports | 200 |
| Services (exports) | 40 |
| Country's X investment abroad | 16 |
| Statistical discrepancy | - 14 |
| Income from Country X's assets abroad | 8 |
| Foreign investment in Country X | 25 |
| Increase in Country X official reserve assets | 4 |
| Income from foreign assets in Country X | 10 |
| Decrease in foreign official reserve assets in Country X | 2 |
| Merchandise imports | 205 |
| Services (imports) | 17 |
| Net unilateral transfers | -9 |

***Exhibit 5***

Based on ***Exhibit 5***, calculate

a) merchandise trade balance.

(1.5 marks)

b) current account balance.

(4 marks)

c) capital account balance.

(1.5 marks)

d) the official reserve balance.

(1.5 marks)

e) balance of payments.

(2.5 marks)

**Part B**

a) Graph the supply and demand for the foreign exchange market, express in terms of ringgit (RM) per pound (£). Show the equilibrium exchange rate at RM5 per pound.

(3 marks)

b) Suppose the U.K economy goes into recessions. All else equal, how is this economic weakness likely to affect the value of pound? Will the ringgit appreciate or depreciate?

(2 marks)

c) Suppose that now the exchange rate between ringgit and pound is fixed at RM5.25 per pound. Show this fixed exchange rate in the diagram drawn in part (a).

(1 mark)

d) Based on (c), has ringgit been overvalued or undervalued? What will happen to the balance of payments account of Malaysia? What will happen to the international reserves of Malaysia if the fixed exchange rate is maintained at RM5.25?

(3 marks)

**[TOTAL 20 MARKS]**

**End of Paper**